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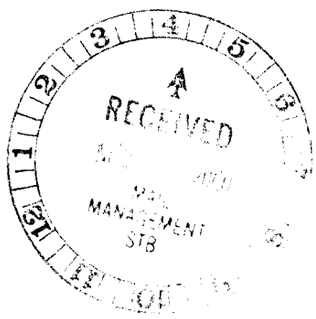
BEFORE THE
SURFACE TRANSPORTATION BOARD

Ex Parte 582 (Sub-No. 1)

PUBLIC VIEWS ON MAJOR RAIL CONSOLIDATIONS



COMMENTS

ON THE

NOTICE OF PROPOSED RULEMAKING

submitted by

THE FERTILIZER INSTITUTE

AND

THE CANADIAN FERTILIZER INSTITUTE

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Dated: November 17, 2000

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The Fertilizer Institute ("TFI") and the Canadian Fertilizer Institute ("CFI") (collectively, "TFI/CFI") respectfully submit these comments in response to the Notice of Proposed Rulemaking ("NPR") of the Surface Transportation Board ("STB") issued on October 3, 2000. TFI/CFI welcome this opportunity to submit their views regarding revisions to the Board's policies on rail mergers. TFI/CFI agree with the fundamental premise of the Board's proposed rules, namely, that the agency's policies on mergers must be substantially revised to meet the needs of rail transportation users and providers in light of a substantially-concentrated rail industry. TFI/CFI also wholeheartedly agree that the Board's approach in future rail mergers must be to "enhance" rather than simply "preserve" competition, and that much more careful

attention has to be given in rail merger applications and administration to the assurance of rail service, oversight, monitoring, and other areas.

However, TFI/CFI believe that the Board's rules are deficient in a number of key areas, and thus should be modified. In particular, TFI/CFI believe that the Board's proposed rules should be significantly revised to provide both railroads and shippers with greater specificity as to how and what competition will be "enhanced," and what will be required, in future rail merger applications. In addition, TFI/CFI believe that the Board should also revise its rules to provide for streamlined dispute resolution processes as a condition of future rail mergers. Finally, TFI/CFI believe that the scope of the Board's rulemaking, which is focused purely on merger policy, is too narrow. Specifically, by focusing purely on conditions in rail mergers, the Board's approach unintentionally would create a serious disparity between the competitive conditions facing merging versus non-merging carriers, to the detriment of both merging carriers and the shipping public. A far better solution, TFI/CFI believe, would be for the Board to revise its rules on rail-to-rail competition, to provide for a level, pro-competitive playing field for all major carriers providing rail transportation service throughout the United States.

I. Identity and Interest of The Fertilizer Institute

The Fertilizer Institute is the national trade association of the fertilizer industry. The Institute, which traces its roots back to 1883, represents more than 250 member companies, including virtually every primary plant food producer, as well as secondary and micronutrient manufacturers, fertilizer distributors and retail dealerships, equipment suppliers and engineering construction firms, brokers and traders, and a wide variety of other companies and individuals involved in agriculture. Many members of TFI utilize rail transportation, and thus have a vital interest in this proceeding. TFI actively participated in the Advance Notice of Proposed Rulemaking, submitting comments at the ANPR stage on May 16, 2000.

II. Identity and Interest of the Canadian Fertilizer Institute

CFI represents the basic manufacturers of nitrogen, phospate, potash, and sulphur fertilizers in Canada, as well as the major retail distributors. Manufacturers include companies in the resource and manufacturing sectors. CFI members produce 24 million metric tons of fertilizers annually, with some 20 million transported by Canada's railways, thus making fertilizers the third largest customer group on those railways. A significant portion of that production is exported to the United States utilizing rail transportation: CFI members ship by rail to 19,000 origin-destination pairs across North America. The annual production value of Canadian fertilizer is approximately $5.5 billion, but Canadian retail sales total only about $2 billion. Canadian fertilizer manufacturers supply approximately 25% of total North American nitrogen fertilizer requirements, and over 90% of the potash requirements. A significant portion of the transportation of Canadian fertilizer production, 30%, is captive to a single railway at the origin. This increases to nearly 60% when the destinations to which Canadian fertilizer production is shipped are considered in the definition of captivity to a single rail carrier. Thus, CFI members have a significant interest in an efficient and competitive North American railway system.

III. The Board's Fundamental Decision to Revise Its Rules to Require "Enhanced Competition" is Correct, But the Board's Rules Need To Be Substantially More Specific In Order To Provide Shippers and Carriers With A Clear Idea of What Will Be Required In Future Merger Applications

The Board's October 3 NPR and the concurring opinion of Commissioner Clyburn both note that the agency's proposed rules represent a "paradigm shift" in the agency's approach to rail mergers. The agency's current policy statement on rail mergers, established in 1979 and modified in 1981, clearly favors rail mergers. The Board's proposed policy, on the other hand, fundamentally makes two significant and welcome changes. First of all, the Board's rules "raise

the bar" for any merger applicant by establishing new procedural and substantive requirements for merging carriers. Thus, the Board's proposed rules move away from the decidedly pro-merger stance contained in the Board's current policies, and shift the balance-point of the agency's policy toward a more neutral position. Second, the most important change proposed by the new policies is to require merging carriers to propose "enhanced competition" in order cure the complex and subtle – but very real – losses in competition that have been permitted in previous mergers through application of the Board's current merger policy.

In TFI/CFI's view, application of the Board's current merger policy over the past five years has produced a decidedly less competitive rail system. Competitive losses have been in two primary areas.

First of all, shippers have lost competition provided by carriers over part of a rail movement, when mergers involving the combination of end-to-end routes have been permitted without ameliorating conditions. For example, if a shipper had been served by Railroad A at origin, but Railroad B and C both could have served the destination, then prior to a merger of Railroads A and B the shipper possessed the benefit of competition over at least a portion of the route, through the competition between Railroad B and C for the traffic as neutral connections to Railroad A. However, a merger of Railroad A and Railroad B eliminated this competition, a loss that the agency's flawed application of the so-called "one lump theory" did not even recognize.

Second, rail mergers of the size and scope since those approved since1994 have vastly reduced the amount of potential leverage provided by geographic competition, as carriers with much broader size and scope began to serve more and more of the producing and consuming regions for various commodities.

The Board's proposed rules clearly represent a welcome departure from these policies. For example, in the NPR, the agency has called for carriers to preserve existing gateways and to

provide for the continued opportunity to enter into contracts for one segment of a movement as a means of gaining the right to separately to pursue rate relief for the remainder of the movement (proposed §1180.1(c)(2)). In proposing these changes, the agency has impliedly discarded the "one lump" theory. And in proposed §1180.1(c), the Board for the first time explicitly recognizes that mergers can result (and future mergers will result) in the loss of geographic competition. These are positive changes, and TFI/CFI applaud them.

However, TFI/CFI are very concerned that the Board's proposed rules need to be substantially more specific. While TFI/CFI recognize that the Board is acting at the level of broad policy and therefore needs to provide for a certain amount of flexibility in its rules to cover situations as they arise, TFI/CFI believe that the proposed rules are so vague as to provide neither shippers nor carriers with clear notice of what is required, and what will be expected, in the area of "enhanced competition." Moreover, the vagueness of the rules is such that TFI/CFI are extremely concerned that applicant carriers in future mergers might give only lip service to key areas of "enhanced competition" because the vagueness of the proposed rules would permit them to do so. In other words, TFI/CFI believe that the Board has to strike a proper balance between flexibility and broad coverage, on the one hand, and specificity on the other. TFI/CFI believe that the proper balance between flexibility and specificity has not been struck in the proposed rules, and therefore TFI/CFI urge the Board to revise the proposed rules to provide for further specificity as to what will be expected of applicant carriers in the area of "enhanced competition" in the future.

There are three areas upon which the Board should focus in making its proposed rules more specific.

First, although the Board's proposed rules specify in a number of places that merger applications must include provisions for "enhanced competition" (see *e.g.*, proposed §1180.1(c)),

the agency's proposed rules never clearly specify that such "enhanced competition" must include provisions for enhanced rail to rail competition. This is an extremely serious lack. Rail carriers in all past mergers have touted the "enhanced competition" that the proposed merger would provide to truck and barge competitors: indeed, such "enhanced competition" between modes was largely the rationale upon which past merger applications were based, and largely the rationale upon which they were approved. But enhanced intermodal competition would do nothing to cure the anti-competitive effects noted above (*i.e.,* loss of segment competition and loss of geographic competition), and if future merger policy is to truly be different from past merger policy, the Board's rules must specific that "enhanced competition" must provide for enhanced rail to rail or intramodal competition in a significant way.

Thus, TFI/CFI suggest that, at a minimum, the fourth sentence of proposed §1180.1(c) be revised to read: "To maintain a balance in favor of the public interest, merger applications must include provisions for enhanced competition, including, but not limited to, significant enhancements of rail-to-rail (intramodal) competition in the area affected by the proposed merger." The second to the last sentence of proposed §1180.1(a) should replace the words "enhanced competition" with the words "enhanced intramodal competition." Finally, the second to the last sentence of proposed §1180.1(d) should also be revised so that the term "enhanced competition" should be replaced with the term "enhanced intramodal competition."

Second, TFI/CFI believe that the Board should revise its proposed merger rules to include examples of enhanced "rail to rail" competition that the Board expects applicant carriers to consider when submitting an application to the agency. Specifically, TFI/CFI suggest that the wording of proposed §1180.1(c)(2)(iv) be revised as follows:

> "Enhanced competition. Applicants shall propose conditions for enhanced competition, including but not limited to enhanced rail to rail competition, in all or major parts of the geographic area affected by the proposed merger. Such

> proposals may include provisions for enhanced reciprocal switching in terminal areas or at interchanges; commitments to provide contract and common carrier rates to interchanges; elimination of existing and future barriers by short lines to provide competitive rail service; establishment of terminal carriers serving all line-haul railroads serving an area; and similar proposals."

Finally, TFI/CFI believe that the wording of the fourth sentence of proposed Section 1180.1(a) should be revised to clarify what appears to be an unintended ambiguity in the proposed rules. That sentence states that the Board "does not favor" consolidations that reduce the railroad and other transportation alternatives "unless there are substantial and demonstrable public benefits to the transaction that cannot otherwise be achieved." This wording suggests that the Board would favor consolidations that reduce railroad and other transportation alternatives where there are substantial public benefits. But such an interpretation (permitted by the proposed wording) would be flatly inconsistent with sound public policy, and inconsistent even with the Board's past practice. Specifically, the Board should make clear that, where a reduction in competition can be specifically proved, then such reductions in competition should be cured as part of the Board's requirements for approval of the proposed merger. Thus, TFI/CFI believe that this wording should be clarified, by changing the proposed rule so that it simply states that the Board "does not favor consolidations that reduce railroad and other transportation alternatives." Such wording would be consistent with the Board's call for "enhanced competition," and would make clear that where there is a reduction in competitive alternatives, these must be cured before a proposed transaction can be approved.

IV. Approval of Any Future Rail Consolidations Should Include a Condition Requiring the Merging Carriers to Provide Mandatory Expedited Arbitration to Resolve Service Disputes and Disputes Over Application of the Board's Conditions In Specific Cases

TFI/CFI strongly believe that the current mechanisms for resolving disputes between shippers and carriers are seriously in need of reform. After the "meltdown" of the UP/SP in 1997

and the service interruptions experienced after the NS/CSX/Conrail transaction, shippers had to resort to the courts to obtain redress -- a lengthy and expensive proposition -- and one which most shippers, and particularly small shippers, simply could not afford. While American business has moved toward inexpensive private methods for quickly resolving commercial disputes, such as mediation and arbitration, rail carriers have never generally consented to arbitration of disputes with shippers.

TFI/CFI strongly believe that the Board should include in its rules a requirement that applicant carriers must agree to mandatory, expedited arbitration, at the shipper's choice, of any disputes over rail service arising within a specified time (*e.g.,* two years) of the implementation of a major merger transaction, and any dispute (regardless of when that dispute arises) over the application of any merger condition in a specific case. (General disputes over the meaning of a merger condition, or other broad policy disputes, would be resolved by the Board in the first instance). Such a requirement, TFI/CFI believe, would provide to shippers an accessible and usable process for resolving problems that might flow from a merger.

V. The Approval of Any Future Consolidation Should Be Accompanied By A Change in the Board's Rules on Terminal Access Through Reciprocal Switching

TFI/CFI support the Board's overall policy change that would give a heightened emphasis to enhancing competition in the context of mergers. However, TFI/CFI are concerned that, by focusing purely on merger policy to accomplish this objective, the agency is creating an "unlevel playing field" for carriers and shippers. Specifically, if two carriers decide to merge, under the Board's proposal they must propose "enhanced competition" as part of their merger application. Assuming that the Board clarifies, as requested by TFI/CFI above, that this requirement must include enhanced rail to rail competition, then the two merging carriers must provide some type of access to their systems. However, while the two merging carriers will be

required to provide some access to their systems, other carriers will not be so obligated. Thus, the merging carriers will be unable to compete for traffic on the systems of non-merging carriers. Not only will this result in a significant disincentive for carriers to merge (particularly given the vagueness of the proposed rules as to what quantum of "enhanced competition" will be necessary to win agency approval of a proposed combination), but will also result in an inequitable situation for shippers on the non-merging versus merging carriers.

Thus, TFI/CFI believe that significantly-increased rail-to-rail competition should include the right to reciprocal switching within a specified distance of a terminal, and to implement this change, the Board should reevaluate its extremely restrictive competitive access rules, under which no shipper has ever succeeded in a competitive access case, to provide for such increased reciprocal switching access immediately. At a minimum the Board should commit to reopen its Ex Parte 441 rules when the next merger is proposed between two current Class I carriers. Only in this way will the competitive benefits of at least a form of "enhanced competition" through reciprocal switching be applied not just to the shippers on the lines of the merging carriers, but to all other shippers as well.

VI. TFI/CFI Comments On Other Proposed Changes

Without exhaustively discussing all of the Board's proposals, TFI/CFI desire to comment briefly on several of the Board's proposed changes.

A. Preservation of Existing Gateways and Preservation of Contract Exception

In proposed rule Section 1180.1(c)(2), the Board proposes to require merger applicants to explain how they would at a minimum preserve existing competitive options such as the use of

major existing gateways, and the opportunity to enter contracts for one segment of a movement as a means of gaining the right to separately pursue rate relief for the remainder of a movement.

TFI/CFI applaud these changes. However, these organizations believe that, with respect to major existing gateways, the Board's rules should make clear that carriers must explain how they would preserve the routing over such gateways not just physically (*i.e.,* by permitting routing over the gateway), but also economically, that is, by insuring that the rate charged to the gateway permits competition over the remainder of the movement. This could be done, for example, through the merging carriers' promise to preserve existing rate relationships, and agreeing in advance to expedited, mandatory arbitration of rate disputes to the gateway.

B. Service Assurance Plans

TFI/CFI applaud the Board's development of a requirement that carriers include a service assurance plan in their merger application. As noted above, TFI/CFI believe that these plans should provide for mandatory, expedited arbitration of any service disputes, at the shipper's election. In addition, the Board should clarify in its final rules that any remedies in a service assurance plan should be in addition to, and should not replace, any remedies that the shipper might have against the carrier as part, for example, of a shipper's contract with the carrier. TFI/CFI want to insure that the inclusion of a carrier's service assurance plan as a condition of the merger, combined with the agency's authority to exempt a merger from the force of other law, would not unintentionally act of strip a shipper of existing rights.

C. Increased Monitoring and Oversight

TFI/CFI support the Board's call for increased monitoring and oversight. In particular, TFI/CFI believe that the Board is correct in requiring carriers to provide baseline, "benchmark" data, so that shippers may have a clear idea of how a merger is actually progressing. However,

TFI/CFI believe that, as part of this requirement, applicant carriers should be required to provide information on transit times over major corridors for the year prior to the application, and then should provide that information following the merger. Transit time information is the most important and direct determinant of the health of a carrier's service, and TFI/CFI are concerned that the Board in its proposed rules appears to be relying too heavily on "indirect" indicia of service such as dwell time, system average train speed, etc. TFI/CFI would note that CSX Transportation Company has recently announced a system whereby shippers can obtain transit time information between major origin and destination areas on its system. This shows that such a system is feasible, and that such a system is not competitively harmful.

D. Examination of Downstream Effects

TFI/CFI support the Board's call for an examination of "downstream" effects. However, these organizations believe that the Board should give prospective applicants a clearer idea of the extent to which such "downstream" effects should be discussed, and the extent to which possible combination of carriers should be examined. Finally, TFI/CFI support Commissioner Burkes' call for an examination not only of "downstream" effects, but also of so-called "upstream" effects, that is, the effect of a proposed merger on the conditions imposed in a prior merger.

VII. Conclusion

TFI/CFI appreciate the opportunity to make their views known to the Board, and respectfully requests the Board to consider these comments as it develops its rules in this proceeding.

Respectfully submitted

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November 17, 2000

Certificate of Service

I hereby certify that I have on this 17th day of November 2000 served a copy of the foregoing Comments on all parties identified in the Board's order in this proceeding, as required by the Board's order and rules of practice.